FIRST LIGHT

17 February 2023

RESEARCH

BOB ECONOMICS RESEARCH | CURRENCY OUTLOOK

INR to remain steady

NESTLE INDIA | TARGET: Rs 22,860 | +16% | BUY

Investing for growth

MARUTI SUZUKI | TARGET: Rs 9,989 | +13% | HOLD

Focus shifts to high-margin segment

CAPITAL GOODS | Q3FY23 REVIEW

Execution trends robust

Daily macro indicators

Indicator	14-Feb	15-Feb	Chg (%)
US 10Y yield (%)	3.74	3.80	6bps
India 10Y yield (%)	7.37	7.35	(2bps)
USD/INR	82.76	82.80	0.0
Brent Crude (US$/bbl)	85.6	85.4	(0.2)
Dow	34,089	34,128	0.1
Hang Seng	21,114	20,812	(1.4)
Sensex	61,032	61,275	0.4
India FII (US$ mn)	**13-Feb**	**14-Feb**	**Chg ($ mn)**
FII-D	91.0	(63.9)	(154.9)
FII-E	181.0	198.6	17.6

Source: Bank of Baroda Economics Research

SUMMARY

INDIA ECONOMICS: CURRENCY OUTLOOK

Dollar rally resumed once again as bets of more Fed rate hikes reemerged. Investors are now expecting two more rate hikes, implying a terminal Fed fund rate above 5.1% (Fed's projection Dec'22). This put pressure on all major global currencies. INR too depreciated by 1.1% in Feb'23, reversing the gains it made at the start of the year. Nevertheless, INR will find some support from improving balance of payments dynamics and stable oil prices. Interestingly, India's trade deficit fell to a 12-month in Jan'23 as imports declined more sharply than exports. On the other hand, services exports remained buoyant. FPI flows though negative, may also end FY23 on a positive note which will further support INR. We expect a range of 82-83/$ for USD/INR in the near-term.

Click here **for the full report.**

NESTLE INDIA

- CY22 revenue increased 14.5% YoY with broad-based growth across categories
- Strategy of penetration-led volume growth along with investment and execution in RURBAN yielding results
- We assume coverage with BUY and a TP of Rs 22,860, set at 67x CY24E EPS

Click here **for the full report.**

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MARUTI SUZUKI

- Q3 gross margin stays healthy at 27% (25% in Q3FY22) due to softer raw material cost and better synergies; realisations drive sales
- Two new SUVs launched with a target of achieving leadership in the high-end SUV segment by FY24
- Growth outlook healthy but priced in; maintain HOLD with a new TP of Rs 9,989 on rollover (vs. Rs 9,933 earlier)

Click here for the full report.

CAPITAL GOODS: Q3FY23 REVIEW

- Strong execution aided 18% YoY revenue growth for our capital goods coverage in Q3 (21% ex-LT) despite supply chain challenges
- Margins and pricing power showed resilience with aggregate gross/ EBITDA margin up 280bps/30bps YoY
- Q4 to be execution-heavy. Structural tailwinds from automation and digitalisation buoy sectoral outlook; we prefer LT, SIEM and AIAE

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CURRENCY OUTLOOK

16 February 2023

INR to remain steady

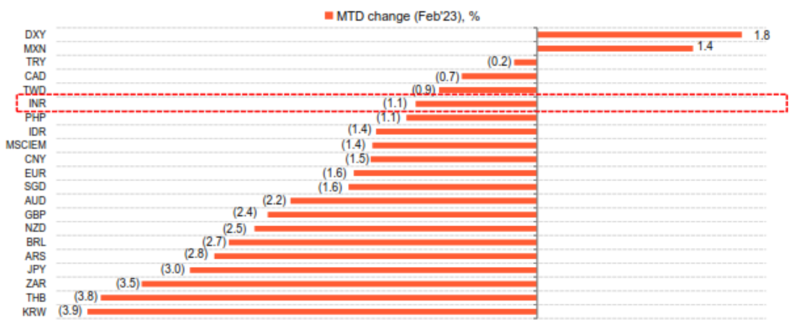
Aditi Gupta
Economist

Dollar rally resumed once again as bets of more Fed rate hikes reemerged. Investors are now expecting two more rate hikes, implying a terminal Fed fund rate above 5.1% (Fed's projection Dec'22). This put pressure on all major global currencies. INR too depreciated by 1.1% in Feb'23, reversing the gains it made at the start of the year. Nevertheless, INR will find some support from improving balance of payments dynamics and stable oil prices. Interestingly, India's trade deficit fell to a 12-month in Jan'23 as imports declined more sharply than exports. On the other hand, services exports remained buoyant. FPI flows though negative, may also end FY23 on a positive note which will further support INR. We expect a range of 82-83/$ for USD/INR in the near-term.

Movement in global currencies

Global currencies once again depreciated as dollar dominance returned in Feb'23. The month started off with hawkish comments from several Fed officials, batting for higher rates cautioning that the battle against inflation has not been fully won. Reinforcing this view, US CPI data showed that prices increased on a MoM basis. This was followed by a stronger than expected retail sales report suggesting underlying momentum in demand. Thus, the case for more rate hikes by the Fed has strengthened and the possibility of the so-called Fed pivot has diminished even more. Market expectations of the Fed terminal rate have seen upward revisions to range of 5.25%-5.5%. Interestingly, this is above Fed's own projection of a terminal rate of 5.1% (as given in SEP Dec'22). Hence, dollar once again resumed its upward rally at the cost of other global currencies.

Figure 1: Global currencies fell in Feb'23



Source: Bloomberg, Bank of Baroda Research, Data as of 15 Feb 2023 | Note: Figures in bracket denote depreciation against USD

Most global currencies depreciated against the dollar in Feb'23 with losses ranging from 0.2% (Turkish Lira) to 3.9% (Korean Won). Amongst advanced economy (AE) currencies, while EUR depreciated by 1.6%, GBP fell by 2.4%. Cooling inflation and expectation of smaller rate hikes by BoE drove losses in GBP. JPY continued to remain under pressure and dropped by 3%, as the new BoJ Governor nominee deemed the central bank's ultra-loose monetary policy stance as appropriate, suggesting that the policy divergence between BoJ and Fed is likely to sustain.

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BUY
TP: Rs 22,860 | 16%

NESTLE INDIA | Consumer Staples | 16 February 2023

Investing for growth

- **CY22 revenue increased 14.5% YoY with broad-based growth across categories**
- **Strategy of penetration-led volume growth along with investment and execution in RURBAN yielding results**
- **We assume coverage with BUY and a TP of Rs 22,860, set at 67x CY24E EPS**

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Robust growth across urban and rural India: NEST's domestic revenue increased 14% YoY in Q4CY22 with a healthy balance between volume and pricing growth. Export revenue grew 17% YoY. In the domestic market, NEST did well in the large metros and mega cities, and continued to see robust growth across smaller towns and rural markets.

Strong performance in key businesses: The prepared dishes and cooking aids businesses continued strong growth momentum in Q4, buoyed by 'Maggi Noodles' and 'Maggi Masala-ae-Magic' which were backed by strong consumer engagement and media campaigns. 'Milkmaid' performed well while milk products continued to face challenges due to the unprecedented rise in milk prices. NEST gained market share and delivered robust growth in the confectionary business driven by 'Kitkat' and 'Munch'.

Margin improves sequentially: NEST's gross profit margin contracted by 200bps YoY in Q4CY22 but expanded sequentially by 220bps QoQ even though prices of key commodities such as cereals, grains and coffee remain at a 10-year high. EBITDA margin at 22.9% expanded 110bps QoQ and remained flat YoY.

Innovation and new product launches: The company has launched over 110 products in the last seven years and has ~30 more in the pipeline. Revenue contribution from new launches has improved gradually, with products introduced since 2015 now contributing 5.4% to sales. Premiumisation remains key for the company and it is accordingly launching millet products under three brands – Ceregrow, A+, and Maggi.

BUY, TP Rs 22,860: NEST's strategy of penetration-led volume growth is yielding results. We expect the company to sustain its growth momentum underpinned by continued investments in innovation and premiumisation, expansion of its direct reach with a focus on rural markets, and forays into newer categories. The stock is trading at 65.8x/57.5x CY23E/CY24E EPS. We assume coverage with BUY and value the stock at 67x CY24E EPS, translating to a TP of Rs 22,860.

Ticker/Price	NEST IN/Rs 19,629
Market cap	US$ 22.9bn
Free float	37%
3M ADV	US$ 13.2mn
52wk high/low	Rs 21,050/Rs 16,000
Promoter/FPI/DII	63%/12%/25%

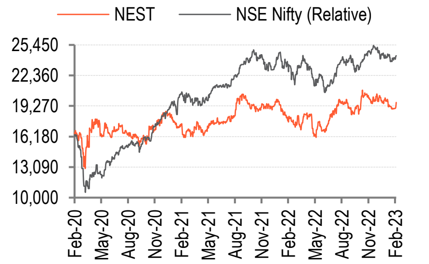
Source: NSE | Price as of 16 Feb 2023

Key financials

Y/E 31 Dec	CY22A	CY23E	CY24E
Total revenue (Rs mn)	1,68,969	1,85,923	2,05,890
EBITDA (Rs mn)	37,125	44,859	51,879
Adj. net profit (Rs mn)	23,905	28,775	32,897
Adj. EPS (Rs)	247.9	298.5	341.2
Consensus EPS (Rs)	247.9	306.6	350.9
Adj. ROAE (%)	97.2	99.2	96.7
Adj. P/E (x)	79.2	65.8	57.5
EV/EBITDA (x)	51.0	42.2	36.5
Adj. EPS growth (%)	1.5	20.4	14.3

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

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HOLD
TP: Rs 9,989 | ⮝ 13%

MARUTI SUZUKI | Automobiles | 16 February 2023

Focus shifts to high-margin segment

- **Q3 gross margin stays healthy at 27% (25% in Q3FY22) due to softer raw material cost and better synergies; realisations drive sales**
- **Two new SUVs launched with a target of achieving leadership in the high-end SUV segment by FY24**
- **Growth outlook healthy but priced in; maintain HOLD with a new TP of Rs 9,989 on rollover (vs. Rs 9,933 earlier)**

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Revenue driven by healthy realisation: MSIL's Q3FY23 revenue grew 25% YoY (-3% QoQ) to Rs 290bn supported by an 8% YoY increase in volumes (-10% QoQ on a high base). Net blended realisation per vehicle (NRPV) came in at Rs 623k (+16% YoY/+8% QoQ).

Margins improve on softer commodity prices: Raw material cost softened following better synergies (operating leverage) at 73% of sales to Rs 211bn vs. Rs 175bn in Q3FY22. This helped gross margin improve 300bps YoY to 27.3%. Other expenses declined QoQ to stand at 13% of sales. In addition to cost savings, favourable currency movement and a better product mix helped EBITDA to grow 82% YoY to Rs 28.3bn and EBITDA margin to rise 350bps YoY to 9.8%.

Focused on achieving leadership in SUVs: MSIL launched two new SUVs – 'Jimny' and 'Fronx' – and aims to achieve leadership in the segment by FY24. The company has showcased a concept electric SUV 'eVX' (launch by 2025). It has commenced exports of 'Grand Vitara' and aims to sell it in over 60 countries.

Capacity expansion and capex: MSIL is planning capacity expansion to 2.5mn units which includes 0.1mn units of brownfield capacity in Manesar (Haryana) by FY24. A new facility at Kharkhoda in Haryana will contribute from FY25 (0.25mn units). Management plans to spend Rs 70bn in FY23 (Rs 35bn incurred in H1FY23) which includes R&D and maintenance-related capex.

Maintain HOLD: We expect MSIL to report a revenue/EBITDA/PAT CAGR of 19%/43%/48% over FY22-FY25, with gross margin of 27% and EBITDA margin of 11% for both FY24/FY25 as input costs ease and realisations gain traction. EPS is forecast at Rs 331/Rs 406 and ROE/ROCE at 15-16% by FY25. Despite the upbeat growth outlook, we maintain HOLD as the current valuation of 21x FY25E EPS partly prices in the positives, leaving limited upside. We roll valuations over to FY25E and value MSIL at 25x P/E, a marginal discount to its 10Y average, for a revised target price of Rs 9,989 (vs. Rs 9,933).

Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	MSIL IN/Rs 8,805
Market cap	US$ 32.2bn
Free float	44%
3M ADV	US$ 54.1mn
52wk high/low	Rs 9,769/Rs 6,537
Promoter/FPI/DII	56%/23%/16%

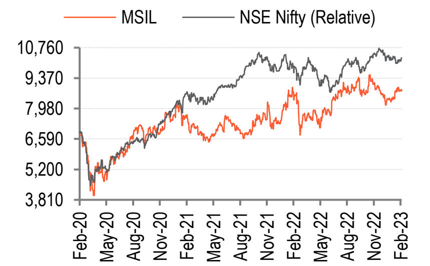
Source: NSE | Price as of 16 Feb 2023

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	882,956	1,127,358	1,302,099
EBITDA (Rs mn)	57,012	103,263	140,889
Adj. net profit (Rs mn)	37,662	70,352	100,019
Adj. EPS (Rs)	124.7	232.9	331.1
Consensus EPS (Rs)	124.7	290.5	366.4
Adj. ROAE (%)	7.1	12.5	15.1
Adj. P/E (x)	70.6	37.8	26.6
EV/EBITDA (x)	46.3	25.4	18.6
Adj. EPS growth (%)	(11.0)	86.8	42.2

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

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CAPITAL GOODS | Q3FY23 Review | 16 February 2023

Execution trends robust

- **Strong execution aided 18% YoY revenue growth for our capital goods coverage in Q3 (21% ex-LT) despite supply chain challenges**
- **Margins and pricing power showed resilience with aggregate gross/ EBITDA margin up 280bps/30bps YoY**
- **Q4 to be execution-heavy. Structural tailwinds from automation and digitalisation buoy sectoral outlook; we prefer LT, SIEM and AIAE**

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Execution momentum continues: Despite supply chain challenges, capital goods players under our coverage displayed impressive project execution in Q3FY23, clocking revenue growth of 18% YoY (21% ex-LT). Barring Hitachi Energy and KKC, most companies adeptly navigated the bottlenecks arising from chip and component shortages. Moreover, aggregate order inflow for our coverage has been robust, growing 13% YoY, and LT's intake at Rs 607bn surpassed expectations.

Margins resilient: Our capital goods universe has demonstrated resilience in the face of inflationary trends, indicative of pricing power and strategic product placement. Ex-EPC (engineering, procurement and construction) players, gross margin expanded by 280bps YoY in Q3. Though cost pressures appear to be abating, the issue of further supply chain constraints amid reopening in China has emerged as a fresh challenge, possibly exacerbating existing component shortages. This conundrum has been flagged by KKC, ABB and Hitachi. Aggregate EBITDA margin rose 30bps YoY, and the ex-EPC margin has swelled 450bps YoY.

Expect a strong Q4: We expect Q4FY23 to be an execution-heavy quarter with robust order flows. LT has guided for revenue and order inflow growth of 13-15% YoY which looks achievable. Contrary to earlier expectations of weakness, the sector has seen relatively healthy exports, particularly from KKC's perspective. In addition, semiconductor shortages are expected to ease, as per earnings commentary from global parent companies ABB and Honeywell.

Retain positive sector outlook: We maintain a positive outlook on the capital goods sector, buoyed by visibility from the government's capex-heavy budget and the likelihood of gradual margin improvement as supply bottlenecks ease. Moreover, we believe the sector is poised to benefit from structural demand tailwinds in the areas of automation, digitalisation and electrification, with product-based companies set to thrive in particular. Against this backdrop, we retain our bullish view on key players LT (BUY, TP Rs 2,440), SIEM (BUY, TP Rs 3,800) and AIAE (BUY, Rs 3,300).

Recommendation snapshot

Ticker	Price	Target	Rating
ABB IN	3,150	3,220	HOLD
AIAE IN	2,818	3,300	BUY
KECI IN	479	500	HOLD
KKC IN	1,629	1,600	HOLD
LT IN	2,175	2,440	BUY
POWERIND IN	2,990	3,500	BUY
SIEM IN	3,229	3,800	BUY
TMX IN	2,112	2,200	HOLD

Price & Target in Rupees | Price as of 15 Feb 2023

Capital Goods: Q3 result reviews

Company	Result review link
ABB IN	Q4 beat; retain HOLD on full valuations
AIAE IN	Stellar quarter despite challenging macro
KECI IN	Disappointing quarter – cut to HOLD
KKC IN	Robust quarter; positives in the price
LT IN	Revenue beat; commentary optimistic
POWERIND IN	Chip shortage takes a toll
SIEM IN	Stellar quarter
TMX IN	Scaling back on large project bids

Source: BOBCAPS Research

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Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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